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E.O. 12958: DECL: 03/17/2014

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SUBJECT: QIZ TALKS: GETTING CLOSER, BUT ISRAELI, EGYPTIAN

NEGOTIATORS DEFER CONTENTIOUS INPUT ISSUE TO THEIR MINISTERS

REF: CAIRO 2024 AND PREVIOUS

Classified By: Economic Counselor Ted Mann, Reasons 1.4(B) and (D)

11. (U) This is a joint cable from Embassies Tel Aviv and Cairo.

Summary

12. (C) The third round of Israeli/Egyptian QIZ talks ended without an agreement on March 17 in Jerusalem. As in the previous discussions in Jerusalem and Cairo, the stumbling block remained the minimum Israeli content requirement for any goods produced in future Egyptian QIZs. Each side made a single additional improvement over its final offer from the second round of talks on March 11 in Cairo (reftel), but it was not enough to bridge the gap. They two sides agreed that, after three rounds of talks, they had achieved all they could on the content issue. They agreed to defer the issue to their respective ministers, Israeli Vice Premier Ehud Olmert and Egyptian Minister of Foreign Trade Youssef Boutros Ghali. No date was set for the ministers' dialogue, which the negotiators agreed could take place either by phone or in a face-to-face meeting sometime between March 25 and April 3. The two delegations also failed to reach agreement on whether the two governments should submit their QIZ proposal to the USG jointly or separately. As in the previous meeting, the atmosphere was cordial, and the two delegations expressed satisfaction with the day's progress. End summary.

The Newest Offers

13. (C) Egyptian negotiator Sayed Elbous said the GOE would now accept 10.5 percent minimum Israeli content for the first two years. Thereafter the minimum content should drop to 8 percent. In the previous meeting, Elbous said Egypt would accept 9 percent for the first two years and 8 percent thereafter. GOI negotiators Gabby Bar and Yair Shiran offered two options. In the first, Israeli content would remain at 12.5 percent permanently. In the second, Israeli content would be 13 percent for the first two years and 12 percent thereafter. During the previous week's talks in Cairo, the GOI had suggested starting at 14.5 percent with a reduction to 11.7 percent over the course of four years. The Israeli content requirement remains the most contentious issue because Israeli inputs are considered more expensive than those available from other sources.

The QIZ's Impact on Israel

14. (C) The issue of input percentages, and the brief exchange of offers, came near the end of a day dominated by a drawn out discussion over the negative impact that Egyptian QIZs would have on some parts of the Israeli textile industry. As in the second round of talks in Cairo, the discussion, attended in full by EconOffs from Embassies Cairo and Tel Aviv, was cordial, although the GOE's Elbous expressed some impatience over the fact that the Israelis did not broach the content issue until late in the day. Bar and Shiran explained at length that Israel recognized the political and economic benefits stemming from QIZ cooperation with Egypt. However, they also said that Egyptian QIZs would create competition for Israeli firms, and that "thousands" of jobs would probably be lost because large Israeli textile companies were looking to move production to Egypt if the two countries signed a QIZ agreement. (Note: Our discussions with Israeli industry sources suggest that the losses would be more in the neighborhood of hundreds of jobs, but particularly painful as they would be in economically hard-hit developments towns like Kiryat Gat. End note.) Elbous encouraged the GOI to recognize that traditional textile manufacturing had no future in a high-cost country

like Israel, and that competition on the world's markets would force the industry's demise with or without Egyptian QIZs. The GOI should see the opportunities for Israeli suppliers, and recognize the political benefits that increased business and governmental contacts between the two countries would bring to Israel.

Negotiators Finally Broach Other Issues

15. (C) After agreeing that they could not reach a consensus on the minimum Israeli input requirement, the two sides touched upon, for the first time since direct negotiations began in January, other issues related to the establishment of Israeli/Egyptian QIZs. Another sticking point dating back to last year's informal discussions between the two governments -- the manner in which the two governments should formally submit their QIZ proposal to the USG -- was discussed but not solved. Elbous suggested that each side send separate letters to the USG requesting recognition of certain industrial zones as QIZs. The GOI's Bar insisted that the two trade ministers write a joint letter. Bar received strong support from MFA Director for Middle East Economic Affairs Ilan Baruch, who was also present at the meeting. Baruch said the issue was of critical importance for Israel, since it would demonstrate the two governments' intention of closer relations. Elbous agreed to discuss the Israeli proposal with his political leadership.

GOI Suggests New Model for Calculating Input Requirement

16. (C) Bar also proposed a new model for calculating how future Egyptian QIZ factories met the minimum Israeli input requirement. In Jordanian QIZ factories, Bar explained, each piece of produced apparel had to contain the minimum level of Israeli inputs. This system was inflexible for the factories and created administrative headaches for the government officials administering the program, he told Elbous. Bar said the GOI would be satisfied if QIZ companies or individual factories purchased the minimum level of Israeli inputs on a quarterly basis. Missing the minimum requirement on individual production batches would be acceptable to the GOI if this were balanced out by other batches containing more than the minimum input percentage. Elbous said the GOE would be open to such suggestions. Both sides told EconOffs that they might ask USG Customs experts to participate in future meetings where technical issues are discussed. Bar and Elbous agreed, however, that another face-to-face meeting made little sense until their respective political leaders had found a compromise on the Israeli content issue.

Comment

17. (C) After a long day of negotiations, all participants showed visible relief after both sides had made their sole offer on minimum Israeli content and decided to refer the contentious issue to their superiors. Both the Israeli and Egyptian industry representatives who were on hand to act as informal consultants also seemed relieved and happy with this result. They denied there was some pre-arranged Ministerial fix in the offing, but seemed to believe that once the Ministers got directly involved, larger political imperatives would prevail and yield a result acceptable to both sides. End comment.

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